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# U.C.C. Survey: General Provisions, Bulk Transfers, and Documents of Title

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# Uniform Commercial Code Annual Survey: General Provisions, Sales, Bulk Transfers, and Documents of Title

By *Fairfax Leary, Jr.\** and *David Frisch\*\**

## GENERAL PROVISIONS

### CONFLICT OF LAWS

As in the past, there were no significant developments or trends in the few decisions on conflict of laws points. The text of U.C.C. section 1-105,<sup>1</sup> the Code's general choice-of-law provision, speaks comprehensively of "the transaction." Yet recent cases and a draft of the proposed Personal Property Leasing Act<sup>2</sup> take an issue-oriented approach, thus giving the parties greater freedom to specify choice of law. Following the formulation in section 187 of the *Restatement (Second) of the Conflict of Laws*, the draft Leasing Act supports party choice in the absence of some significant forum policy that requires overriding that choice.<sup>3</sup>

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Don L. Baker of Austin, Texas, and Fairfax Leary, Jr. are cochairmen of the Subcommittee on General Provisions, Sales, Bulk Transfers, and Documents of Title. The following members of the subcommittee contributed to the writing of this survey: Anthony Adams, Marvin E. Barkin, Calvin W. Corman, Joseph J. Gazzoli, Lawrence B. Hunt, Dennis S. Kayes, Ann Lousin, Susan M. Mann, John E. Murray, Jr., Jeffrey L. Raney, Michael D. Strobechn (assisted by Beverly A. Zimmerman), Victor A. Vilaplana, and William R. Waddell.

*Editor's note:* This article and the one that follows are a continuation of the survey of 1984 developments under the Uniform Commercial Code. Other sections of the survey appeared in the May 1985 issue of *The Business Lawyer*.

1. All references to the U.C.C. are to the Uniform Commercial Code, 1978 Official Text.

2. The Leasing Act is being drafted under the aegis of the National Conference of Commissioners on Uniform State Laws (NCCUSL). The reporters are Ronald DeKoven, Esq. of the New York bar and Professor James A. Martin of the Michigan Law School. The draft was submitted for a first reading to the commissioners at their summer 1984 meeting at Keystone, Colorado, July 27–August 3, 1984. It has not been approved by the commissioners, the committee, or the reporters.

3. Draft of Personal Property Leasing Act No. 5, at 20–21 (Mar. 3, 1985) (not approved by the NCCUSL, its subcommittee, or the reporters). The proposed language may not be used to ascertain the legislative meaning of any promulgated final law. Subsection (a) of § 107 of the draft Leasing Act reads as follows:

In the consumer context, the Leasing Act draft, both in choice of law and in choice of forum,<sup>4</sup> negates certain choice-of-law agreements in order to protect consumers from the inconvenience of a distant forum<sup>5</sup> or strange rules of law. In cases considering commercial transactions involving banks, even when U.C.C. section 4-102(2) is not applicable, courts have adopted the law of the state in which the bank is located.<sup>6</sup>

Perhaps consideration should be given to whether both the Code and the proposed Leasing Act should also permit the parties to agree to be governed by the terms of a particular trade practice code, even though it is not, as such, the law of any particular jurisdiction.<sup>7</sup>

In one leasing case, *In re Loop Hospital Partnerships*,<sup>8</sup> the court noted that under U.C.C. sections 9-102 and 9-103, the applicable law could differ depending upon the issue, that is, "repossession and resale" versus "validity," rather than selecting one jurisdiction for the entire transaction, thus apparently adopting an "issue" approach.

In *Hammermill Paper Co. v. Pipe Systems, Inc.*,<sup>9</sup> Hammermill sued Pipe in Pennsylvania for breach of warranty. Seeking indemnification, Pipe impleaded

Subject to subsections (c) and (d), the parties may agree that the law of this State or of another jurisdiction govern their rights and duties under the lease if the particular issue is one that the parties may resolve by agreement under this [Act]. Even if the issue is not one that the parties may resolve by agreement under this [Act], the parties may agree that the law of this State or of another jurisdiction govern their rights and duties under the lease unless:

- (1) the law chosen is that of a jurisdiction having no substantial relationship with the transaction and there is no other reasonable basis for the parties' choice; or
- (2) application of the law chosen would be contrary to the fundamental policy of the jurisdiction whose law would otherwise be chosen by the applicable choice of law rules of this State, including subsection (b).

Subsection (b) directs the court to apply "the law of the jurisdiction that has the most significant relation with the lease." Subsection (c) states a special rule for consumer leases, namely, either the law of the residence of the consumer "at the time the lease agreement becomes enforceable or within 30 days thereafter or in which the goods are to be used." Any other choice is without effect.

4. *Id.* § 108, at 23.

5. *Id.* §§ 107 (c), (d).

6. *Banco Nacional de Desarrollo v. Mellon Bank*, 726 F.2d 87, 37 U.C.C. Rep. Serv. (Callaghan) 1651 (3d Cir. 1984); *Barclays Discount Bank, Ltd. v. Bogharian Bros.*, 568 F. Supp. 1116 (C.D. Cal. 1983); *Israel Discount Bank, Ltd. v. Rosen*, 59 N.Y.2d 428, 452 N.E.2d 1213, 465 N.Y.S.2d 885 (1983).

7. The conflict-of-laws provisions in both the U.C.C. and the Leasing Act make no reference to trade practice. In *Banco Nacional de Desarrollo v. Mellon Bank*, 726 F.2d at 90 n.5, 37 U.C.C. Rep. Serv. at 1655 n.5, the Third Circuit stated that the Uniform Customs and Practices for Documentary Credits did not qualify as "the substantive law of a state" for adoption by the parties.

8. 35 Bankr. 929, 938, 37 U.C.C. Rep. Serv. (Callaghan) 1679, 1692 (Bankr. N.D. Ill. 1983).

9. 581 F. Supp. 1189, 38 U.C.C. Rep. Serv. (Callaghan) 1265 (W.D. Pa. 1984). The court cited *Griffith v. United Air Lines, Inc.*, 416 Pa. 1, 203 A.2d 796 (1964), *Restatement (Second) of Conflict of Laws* § 147, and *Melville v. American Home Assurance Co.*, 584 F.2d 1306, 1311-13 (3d Cir. 1978). In considering the second part of Pennsylvania's analysis and the *Restatement's* flexible two-part analysis, the court found that the issue of products liability law involved policy interests of considerable consequence to Pennsylvania because the damages occurred in Pennsylvania. *See also* *First Nat'l Bank v. Insurance Centers, Inc.*, 560 F. Supp. 1261, 1263 (E.D. Mo. 1983) (citing

its supplier under a distributorship agreement that designated Texas law, and also asserted a products liability claim. The third-party defendant moved for summary judgment based on Texas law and a one-year contractual bar to claims in the distributorship agreement.

The court applied Texas law to the third-party warranty claim and granted the supplier's motion. The distributorship agreement did not govern the strict liability claim, however, and the court turned to Pennsylvania's general choice-of-law rules in tort and strict liability cases. It determined that Pennsylvania law applied. Again, this was an "issue" approach.

## HYBRID SALES AND SERVICE CASES

A distributorship agreement calling for a "host of service responsibilities" nevertheless was subject to article 2 as the "sale of goods was the *raison d'être* of the Agreements."<sup>10</sup> A printing contract was held to be a sale of the finished magazines so that no consideration was needed for a modification under U.C.C. section 2-209.<sup>11</sup>

In other cases, even though the contract was held not to be subject to article 2 either as a service contract<sup>12</sup> or as a federal contract,<sup>13</sup> the provisions of the Code were applied. Of seventeen cases reviewed, fourteen applied the U.C.C. on one basis or another,<sup>14</sup> indicating the need, in the area of commercial service contracts, for more available guidance than the common law provides.

In *Hudson v. Town & Country True Value Hardware, Inc.*,<sup>15</sup> the Tennessee Supreme Court, unlike the courts that applied the U.C.C. at the parties'

*Phillips v. Englehart*, 437 S.W.2d 158 (Mo. Ct. App. 1968), applying the law of a state to which "some element of the contract is properly referable"). The *Insurance Centers* court also likened the U.C.C. § 1-105 tests to the rule of *Seeman v. Philadelphia Warehouse Co.*, 274 U.S. 403 (1927). Section 106(a)(2) of the draft Leasing Act more concretely permits the disregard of the contractual choice-of-law clause when its purpose is to evade a fundamental policy of the otherwise applicable jurisdiction's law.

10. *WICO Corp. v. Willis Indus.*, 567 F. Supp. 352, 37 U.C.C. Rep. Serv. (Callaghan) 20 (N.D. Ill. 1983). An installation contract for components of a cold storage room had as its dominant aspect the sale of the components, the trial court concluded; on appeal, both parties agreed that the U.C.C. applied. *Mayflower Farms v. Tech-Mark, Inc.*, 64 Or. App. 121, 666 P.2d 1384, 37 U.C.C. Rep. Serv. (Callaghan) 25 (1983); *accord O'Keefe Elevator Co. v. Second Ave. Properties, Ltd.*, 216 Neb. 170, 343 N.W.2d 54, 37 U.C.C. Rep. Serv. (Callaghan) 1100 (1984) (wheelchair lift, parties tried as U.C.C. case). In *Bethlehem Steel Corp. v. Litton Indus.*, No. 37 W.D. Appeal Docket 1984 (Pa. Feb. 22, 1985), the Pennsylvania Supreme Court ruled that the U.C.C. applied to a contract for the construction of a 1,000-foot self-unloading vessel that, although immovable during the special construction, would be movable after launching.

11. *Gross Valentino Printing Co. v. Clarke*, 120 Ill. App. 3d 907, 458 N.E.2d 1027, 37 U.C.C. Rep. Serv. (Callaghan) 1460 (1983).

12. *Liberty Fin. Management Corp. v. Beneficial Data Processing Corp.*, 38 U.C.C. Rep. Serv. (Callaghan) 1471 (Mo. Ct. App. 1984).

13. *Clem Perrin Marine Towing, Inc. v. Panama Canal Co.*, 730 F.2d 186 (5th Cir. 1984) (lease and sale of tugboat).

14. Several are not specifically discussed.

15. 666 S.W.2d 51, 38 U.C.C. Rep. Serv. (Callaghan) 6 (Tenn. 1984). There were separate contracts, one for the real estate and one for the personality. The latter was conditioned upon the

behest,<sup>16</sup> consolidated two separate contracts covering the sale of a business and applied the dominant interest test, treating the whole as a sale of real estate breached by the buyer. The court reversed a decision of the court of appeals, which required separate awards of damages for the personalty contract and the real estate contract, and reinstated the trial court's award to the seller of the difference between the total of the two contract prices and the price received by the seller on a subsequent sale to another.

## ARTICLE 2—SALES

### STATUTE OF FRAUDS

One situation not well handled by the Code, in view of its statute of frauds, is the obligation, if any, of a subcontractor submitting an oral offer to be used by a contractor in its bid for a contract.<sup>17</sup> This problem arose in *H.B. Alexander & Son v. Miracle Recreation Equipment Co.*<sup>18</sup> The court refused to allow the supplier to use the statute of frauds to escape from a bad deal. Ignoring certain contentions of the parties,<sup>19</sup> the court concluded that the parties, by their conduct and course of dealing, had waived compliance with the statute of frauds.<sup>20</sup>

The result is correct, but the use of waiver and course of dealing can be faulted.<sup>21</sup> The court would have been on firmer ground had it based its

closing of the land sale. The land sale was conditioned upon the buyer's obtaining financing. Since the buyer's efforts to obtain financing "were inadequate," the trial court found the buyer in default.

16. See *O'Keefe Elevator Co. v. Second Ave. Properties, Ltd.*, 216 Neb. 170, 343 N.W.2d 54, 37 U.C.C. Rep. Serv. (Callaghan) 1100 (1984).

17. U.C.C. § 2-205 on firm offers does not solve the problem, as it requires the irrevocable offer by a merchant to be in a signed writing. Also, many subcontractor-general contractor cases fall outside the Code as service contracts, not sales of goods.

18. 314 Pa. Super. 1, 460 A.2d 343, 36 U.C.C. Rep. Serv. (Callaghan) 750 (1983).

19. Alexander, the general contractor, had, upon receiving the award, sent a vendor's order as an unanswered memorandum to a merchant. Miracle responded by arguing that the order was insufficient because it did not indicate that it was confirming a contract and the clause "to make any agreement valid sign, date and return copy at once. Advise definite shipping date and if by rail or truck" was an impermissible condition precedent. *Id.* at 3 n.2, 460 A.2d at 344 n.2, 36 U.C.C. Rep. Serv. at 751 n.2.

20. Recognizing the importance of the bidding issue, the court said:

It is essential that general contractors be allowed to accept and rely on telephone bids from subcontractors in arriving at their final bids since time is often an important factor. Clearly [Miracle] was aware of this generally accepted custom and in fact often used this practice in its transactions with general contractors.

*Id.* at 5-6, 460 A.2d at 345, 36 U.C.C. Rep. Serv. at 752-53.

21. The relevance of course of conduct, or course of dealing and even usage of trade, lies in their use in determining the meaning to be given to the terms of an agreement, not in making the agreement enforceable in the teeth of U.C.C. § 2-201. Totally ignored by the court was comment 2 to U.C.C. § 1-102, which provides that "the statute of frauds found in Section 2-201 . . . does not explicitly preclude oral waiver of the requirement of a writing, but a fair reading denies enforcement to such a waiver as part of the 'contract' made unenforceable." It is noteworthy that there is no mention of "waiver" in U.C.C. § 1-103.

conclusions on an estoppel exception to the statute of frauds under U.C.C. section 1-103.<sup>22</sup>

The merchant's exception to the statute of frauds, avoided by the court in the preceding case, arose in *Great Western Sugar Co. v. Lone Star Donut Co.*<sup>23</sup> The writing sent by the seller seven weeks after the alleged oral agreement concluded, "This letter is a written confirmation of our agreement. Please sign and return to me the enclosed counterpart of this letter signalling your acceptance of the above agreement."<sup>24</sup>

The court ignored the difference between compliance with the statute of frauds and the benefits of a signed written agreement which would preclude much litigation over its terms. Should it not be possible while confirming an oral contract to try for a written contract in addition? The court laconically ruled that "[a] true confirmation requires no response."<sup>25</sup> This may be true, but to have a written agreement to eliminate potential controversy requires writings signed by both parties.

Perhaps with more careful drafting, the dual purpose can be served. The key may be in the use of the words "signalling your acceptance" of this agreement. What would the judge have done with a sentence requesting a signed return "signalling your concurrence that all of the terms and conditions herein stated are a part of our contract"<sup>26</sup>?

Issues regarding the sufficiency of the writings and whether a check for \$250,000 brought a contract to buy an \$8.85 million aircraft within the partial payment rule of U.C.C. section 2-201(3)(c) arose in *Songbird Jet Ltd. v. Amax, Inc.*<sup>27</sup> The judge ruled incorrectly that the statute requires that one document, on its own, must be "sufficient to indicate that a contract for sale has been made."<sup>28</sup> But the judge agreed that a check for \$250,000 would indeed be

22. A promissory estoppel exception to the statute of frauds has been applied before. See, e.g., *Allen M. Campbell Co., Gen. Contractors, Inc. v. Virginia Metal Indus., Inc.*, 708 F.2d 930, 36 U.C.C. Rep. Serv. (Callaghan) 384 (4th Cir. 1983); *Northwest Potato Sales, Inc. v. Beck*, 37 U.C.C. Rep. Serv. (Callaghan) 1468 (Mont. 1984). See also *Restatement (Second) of Contracts* § 139 (1981); *Annot.—Promissory Estoppel as Basis for Avoidance of Statute of Frauds*, 56 A.L.R.3d 1037 (1974).

23. 567 F. Supp. 340, 37 U.C.C. Rep. Serv. (Callaghan) 35 (N.D. Tex.), *aff'd*, 721 F.2d 510 (5th Cir. 1983).

24. 567 F. Supp. at 342, 37 U.C.C. Rep. Serv. at 37.

25. *Id.* at 342, 37 U.C.C. Rep. Serv. at 38.

26. The imprecision of the English language is indicated here. "Acceptance" can be misunderstood as being used with the meaning "This is an offer needing a legal acceptance." Alternatively, "acceptance" can mean a request for a written concurrence that the "confirmation" correctly stated everything contained therein. Of course, for a memorandum to be "in confirmation," it must use words such as "as per agreement," "in confirmation of," or "sold to buyer." *Howard Constr. Co. v. Jeff Cole Quarries, Inc.*, 37 U.C.C. Rep. Serv. (Callaghan) 1040, 1047 (Mo. Ct. App. 1983).

27. 581 F. Supp. 912, 38 U.C.C. Rep. Serv. (Callaghan) 431 (S.D.N.Y. 1984).

28. *Id.* at 922, 38 U.C.C. Rep. Serv. at 441. The judge overlooked the explanation of the language in comment 1 stating that all "that is required is that the writing afford a basis for believing that the offered oral evidence rests on a real transaction." Fortunately, the one document position is not shared by all courts, nor even by some members of the same court. See, e.g., *East Eur.*

"unintelligible," or at least "extraordinary,"<sup>29</sup> unless referable to an oral agreement of some sort.

Section 2-201(1) clearly states that a sufficient writing must contain a quantity term. *Slocomb Industries, Inc. v. Chelsea Industries*<sup>30</sup> held that a writing is sufficient if it "indicates that the quantity to be delivered under the contract is a party's requirements or output."<sup>31</sup> Unfortunately, not all courts have been so commercially minded when presented with open quantity terms.<sup>32</sup>

## CONTRACT FORMATION

### OFFER AND ACCEPTANCE

There is a difference between "sales in law" and "sales in practice." The Code's attempt to harmonize the two may work well enough for the large organization with batteries of forms and with personnel carefully trained in their use. But for smaller businesses, "one form fits all" seems to be the rule.

*American Bronze Corp. v. Streamway Products*<sup>33</sup> illustrates the chameleon-like nature of purchase order forms. The central element is the purchase order number used for transactional identification and processing. On its face, as worded, the purchase order appears to be an offer.<sup>34</sup> But a professional buyer may use the form in two other ways. One would be as an acceptance of an offer to sell, and some courts have, in certain circumstances, accepted its use for that purpose.<sup>35</sup> Another would be as a confirmation of an oral contract.

*American Bronze* involved four transactions in which the buyer, following what had been done for more than twenty years, "would first call in the order by telephone and then follow it up with a written purchase order at which time [the seller] would begin production."<sup>36</sup>

After three purchase orders were placed, the seller began production and then refused to deliver. Its stated reason was that the buyer had placed with other

*Domestic Int'l Sales Corp. v. Island Creek Coal Sales Co.*, 572 F. Supp. 702, 37 U.C.C. Rep. Serv. (Callaghan) 1030 (S.D.N.Y. 1983).

29. 581 F. Supp. at 923, 38 U.C.C. Rep. Serv. at 442 (citing *Anostario v. Vicinanza*, 59 N.Y.2d 662, 664, 450 N.E.2d 215, 216, 463 N.Y.S.2d 409, 410 (1983) (mem.) (quoting *Burns v. McCormick*, 233 N.Y. 230, 232, 135 N.E. 273, 273 (1922))).

30. 36 U.C.C. Rep. Serv. (Callaghan) 1543 (E.D. Pa. 1983).

31. *Id.* at 1548 (citing *Eastern Dental Corp. v. Isaac Masel Co.*, 502 F. Supp. 1354 (E.D. Pa. 1980)). See *In re Estate of Frost*, 37 U.C.C. Rep. Serv. (Callaghan) 1476 (Mich. Ct. App. 1983), where, in an analogous situation, the court held that "all wood sawable" was a valid quantity term.

32. See generally Bruckel, *The Weed and the Web: Section 2-201's Corruption of the UCC's Substantive Provisions—The Quantity Problem*, 1983 U. Ill. L. Rev. 811.

33. 8 Ohio App. 3d 223, 456 N.E.2d 1295, 37 U.C.C. Rep. Serv. (Callaghan) 687 (1982).

34. See, e.g., *J.B. Moore Elec. Contractor, Inc. v. Westinghouse Elec. Supply Co.*, 221 Va. 745, 273 S.E.2d 553, 30 U.C.C. Rep. Serv. (Callaghan) 1224 (1981).

35. See, e.g., *Earl M. Jorgensen Co. v. Mack Constr., Inc.*, 56 Hawaii 466, 540 P.2d 978 (1975). On the other hand, a purchase order may merely evidence an offer rather than a prior oral contract. See *Nations Enter., Inc. v. Process Equip. Co.*, 40 Colo. App. 390, 579 P.2d 655, 24 U.C.C. Rep. Serv. (Callaghan) 828 (1978).

36. 8 Ohio App. 3d at 227, 456 N.E.2d at 1300, 37 U.C.C. Rep. Serv. at 691.

sellers purchase orders that seller could also have filled. The fourth purchase order was rejected and returned four days after it was placed.<sup>37</sup>

Crucial to a determination of liability on the fourth transaction is what was said by the seller when receiving the telephone order.<sup>38</sup> Apparently, the issue of the fourth transaction was not raised on appeal.<sup>39</sup> If it was, the court's treatment of the previous purchase orders as offers accepted under U.C.C. section 2-206 by the beginning of production precluded a finding that the return of the fourth purchase order was a breach.

*In re Isis Foods, Inc.*<sup>40</sup> is a case in which on receipt of a purchase order, the seller shipped the goods and also sent an invoice containing different terms. Which was the acceptance? The buyer's purchase order was F.O.B. destination, and the invoice contained the term "Our liability ceases upon delivery of the merchandise to the carrier." If the shipment occurred before the seller dispatched the invoice, and there is some indication of this, at best the invoice was a request for modification not accepted by the buyer. If the dispatch of the invoice occurred before the shipment, it could constitute a counteroffer, or if it was construed as or contained "a definite and seasonable expression of acceptance," a U.C.C. section 2-207 question would arise. Interesting, from the viewpoint of contract interpretation, is the court's conclusion that even if part of the contract, "the term in the invoice . . . does not clearly negate the provision that . . . defendant bore the responsibility for delivery of the goods [to buyer]. . . ."<sup>41</sup> Not made clear, however, is just how the two terms could be construed as being in harmony.<sup>42</sup>

37. At one point, the court appeared to find an offer in the purchase order and an acceptance in the beginning of production. Hence, when no production was begun, there was no acceptance. U.C.C. § 2-204(1).

38. Without discussing what was said, the trial court characterized the purchase orders as "confirming a telephone order." Trial Court's Finding of Fact 5 adopted by the court of appeals. 8 Ohio App. 3d at 226, 456 N.E.2d at 1298, 37 U.C.C. Rep. Serv. at 689.

39. It was not discussed, and the court of appeals, after referring to the finding as to the three preceding orders, stated, "We agree and hold that the parties did enter into the three contracts in issue," 8 Ohio App. 3d at 227, 456 N.E.2d at 1300, 37 U.C.C. Rep. Serv. at 692. Added confusion results from the court's discussion of the statute of frauds. First, the court seemed to treat the purchase order as a U.C.C. § 2-201(2) confirmatory memorandum, and then it stated that the seller's acceptance (apparently referring to the beginning of production) "was sufficient to indicate that these contracts for sale had been made." *Id.* at 228, 456 N.E.2d at 1301, 37 U.C.C. Rep. Serv. at 692. This does not seem to fit any of the provisions of U.C.C. § 2-201.

40. 38 Bankr. 48, 38 U.C.C. Rep. Serv. (Callaghan) 1134 (Bankr. W.D. Mo. 1983).

41. *Id.* at 50, 38 U.C.C. Rep. Serv. at 1137.

42. If not in harmony, and if the invoice was sent first, *see id.* at 49, 38 U.C.C. Rep. Serv. at 1136, there would be conflicting terms, and the Code term under U.C.C. § 2-509(1)(b) places the risk of loss on the seller until destination, as the court held. Otherwise, the court might have considered the invoice term an "agreement otherwise" under U.C.C. § 2-509(4). If so, why was it not a "material alteration"? If the shipment occurred first, constituting an acceptance of the purchase order, the invoice could only be a U.C.C. § 2-209(1) request for modification.



*South Hampton Co. v. Stinnes Corp.*<sup>43</sup> adds a desirable gloss to U.C.C. section 2-206(1)(a).<sup>44</sup> Though performance may be a reasonable manner of acceptance, when the particular performance occurs under circumstances that cause the offeror reasonably to doubt whether the performance is intended as an acceptance, a refusal of the offeree to confirm that intention will preclude the performance from operating as an acceptance.

*J. Baranello & Sons v. Hausmann Industries, Inc.*<sup>45</sup> indicates the care with which courts expect the parties to express themselves. The negotiations started with a telephone bid from a subcontractor to supply a bidding contractor with certain wardrobes that differed in only one respect from the state's required design. The subcontractor claimed that its design would meet state approval. It developed that it would not. After much discussion and attempts to gain state approval, the contractor wrote the subcontractor a letter expressly superseding prior letters, specifying that all work would be in accordance with state specifications and increasing the price by \$17,375. The subcontractor replied with a letter three days later indicating that the additional cost of \$17,375 was for "[a]dditional costs for amending specifications, method of assembly and construction of wardrobes to meet F.D.C. [state] requirements."<sup>46</sup> But objection was made to the subcontractor's drawings, and it could not satisfy the state.

When sued, the subcontractor argued that its letter was not intended to constitute an acceptance and that the parties had not reached agreement on the logistics of shipping the wardrobes to a third party who was to supply certain molding. The court ruled that defendant's *subjective* intent was irrelevant, that there was an objective intent to contract, even with a material term left open,<sup>47</sup> and that because of defendant's refusal to comply, the court could fashion a remedy.

43. 733 F.2d 1108, 38 U.C.C. Rep. Serv. (Callaghan) 1137 (5th Cir. 1984).

44. The contract was for a ten-year period. Buyer had an option to cancel if seller did not build certain facilities to bring the oil to buyer by pipeline. Seller had the option to accept the cancellation or offer oil from another source for the balance of the contract. Proper notice of cancellation was given when the facilities were not constructed, but seller refused to accept it and continued deliveries from an alternate source. Buyer inquired whether seller was exercising its option to complete the contract from that alternate source. Seller merely replied that oil was available. After some negotiations between buyer, seller, and the users buying from Stinnes, all buyers cancelled and seller sued; buyer counterclaimed. Seller claimed it had exercised its contract by conduct. The court found otherwise.

45. 571 F. Supp. 333 (E.D.N.Y. 1983).

46. *Id.* at 338.

47. The court quoted from *Kleinschmidt Div. of SCM Corp. v. Futurionics Corp.*, 41 N.Y.2d 972, 363 N.E.2d 701, 395 N.Y.S.2d 151, 21 U.C.C. Rep. Serv. (Callaghan) 422 (1977): "It is no longer true that dispute over material terms inevitably prevents formation of a binding contract. What is true . . . is that when a dispute over material terms manifests a lack of intention to contract, no contract results." 571 F. Supp. at 341. If the term prevents the court from fashioning a remedy, lack of objective intention to contract is conclusive.

## INDEFINITENESS AND OPEN TERMS

Many contract terms left open by the parties can be supplied if the words and conduct of the parties, considered objectively, establish the requisite intent to contract and if there is a reasonably certain basis on which to construct a remedy.

Three cases dealt with the parties' failure to define the duration of their contractual relationship.<sup>48</sup> U.C.C. section 2-309(2) provides that such a contract is valid for a reasonable time though terminable by either party at any time subject to the reasonable notice requirement of U.C.C. section 2-309(3). The cases confirm that the reasonableness of a time period is a question of fact. In one case, the trial judge ruled that termination of a distributorship occurred prematurely.<sup>49</sup> The Ninth Circuit ruled, correctly, that such a contract was terminable at the will of either party. The only requirements were that the notice be sent in good faith and that the reasonableness of the notice period be judged by the amount of time necessary to look for a new source of supply.

*In re Pennsylvania Tire Co.*<sup>50</sup> illustrates the many problems that occur in the termination of a multiproduct distributorship agreement. First, the bankruptcy judge held that since the parties had dealt with each other for ten years, the reasonable period for validity had run. Relying on a clause in the agreement and oral testimony, the judge ruled that the parties had agreed on termination without any prior notice. As to U.C.C. section 2-309(2), he then said, "Indeed it is possible to find that, as between seasoned merchants, certainly an apt description of these parties, termination without prior notice is not commercially unreasonable"<sup>51</sup> and so not unconscionable. Then the judge, relying on pre-Code agency law, buttressed his holding of no liability by stating that "any agreement found to exist is unenforceable for lack of mutuality."<sup>52</sup>

Apparently, a different result could have been reached under U.C.C. section 2-306 had the distributor been given an exclusive territory or had it handled only the supplier's tires.<sup>53</sup> The court did hold that the distributor was entitled to a setoff for future adjustments it would have to make with those who had purchased tires from it and who would, based on past experience, have claims. Also, the supplier was awarded interest on unpaid invoices, but only at the statutory rate of 6% to July 30, 1980, and 8% thereafter,<sup>54</sup> not at the rates of 12% to 20% that it had charged. Interest on past-due invoices was not charged until late in 1979, and no payments of such interest had been made by the

48. *Zidell Explorations, Inc. v. Conval Int'l, Inc.*, 719 F.2d 1465, 37 U.C.C. Rep. Serv. (Callaghan) 466 (9th Cir. 1983); *In re Pennsylvania Tire Co.*, 26 Bankr. 663, 37 U.C.C. Rep. Serv. (Callaghan) 410 (Bankr. N.D. Ohio 1982); *Mayflower Farms v. Tech-Mark, Inc.*, 64 Or. App. 121, 666 P.2d 1384, 37 U.C.C. Rep. Serv. (Callaghan) 25 (1983).

49. *Zidell Explorations*, 719 F.2d 1465, 37 U.C.C. Rep. Serv. 466.

50. 26 Bankr. 663, 37 U.C.C. Rep. Serv. (Callaghan) 410 (Bankr. N.D. Ohio 1982).

51. *Id.* at 670, 37 U.C.C. Rep. Serv. at 419.

52. *Id.* at 671, 37 U.C.C. Rep. Serv. at 419.

53. U.C.C. § 2-306(2) ends the lack of mutuality argument by creating a best efforts obligation on the part of each party.

54. 26 Bankr. at 669; 37 U.C.C. Rep. Serv. at 416.

distributor. Hence, the supplier failed in its attempt to justify its higher-than-statutory rates of interest based on course of performance and the distributor's failure to object.

*Lapeyrouse Grain Corp. v. Tallant*<sup>55</sup> involved farmers delivering grain to a dealer's storage bins under an oral agreement and a course of dealing that the grain was "unpriced," meaning that there was no sale until the farmers fixed the price. No specific pricing date was fixed. The dealer sent checks to the farmers based on its theretofore-undisclosed "cut-off date," a date on which the price was two cents a bushel lower than the day before and eight cents lower than on the following day. The farmers sued in conversion. The court held that the farmers' testimony was sufficient to present a jury question as to whether the arrangement was a bailment or a sale. A judgment in conversion for the farmers was affirmed.<sup>56</sup>

In *Bethlehem Steel Corp. v. Litton Industries, Inc.*,<sup>57</sup> the Pennsylvania Supreme Court affirmed by necessity, on a two-to-two vote, a ruling of no contract. As the trial judge noted with some amazement, "The claim in excess of 95 million dollars, together with a counterclaim, is based on a two-page letter between two giant corporations."<sup>58</sup> The letter, signed at the ceremonial signing of a major contract for the purchase of one vessel, led to a dispute whether it was an enforceable option or merely an agreement to negotiate an option. By its express terms, the letter was "an offer to enter into an option agreement"<sup>59</sup> to have Litton construct one to five additional vessels for Bethlehem. But several terms were left open.<sup>60</sup> Subsequent negotiations on the open terms were unsuc-

55. 439 So. 2d 105, 37 U.C.C. Rep. Serv. (Callaghan) 405 (Ala. 1983).

56. The court said: "We find that the evidence of record concerning the storage agreement is sufficient to present a jury question as to whether the delivery was a bailment or a sale." *Id.* at 109, 37 U.C.C. Rep. Serv. at 408.

57. No. 37 W.D. Appeal Docket 1984 (Pa. Feb. 22, 1985) *aff'd by necessity* 321 Pa. Super. 357, 468 A.2d 748, 37 U.C.C. Rep. Serv. (Callaghan) 1059 (1983). Three supreme court justices took no part; two voted to affirm; and two, to reverse.

58. 321 Pa. Super. at 361, 468 A.2d at 749, 37 U.C.C. Rep. Serv. at 1062.

59. Plaintiff's exh. 4. *Id.* at 363, 468 A.2d at 750, 37 U.C.C. Rep. Serv. at 1062. "We hereby extend to you an offer to enter into an option agreement." *Id.* at 362, 468 A.2d at 750, 37 U.C.C. Rep. Serv. at 1062. Bethlehem replied, "We . . . accept your offer of an option." *Id.* at 364, 468 A.2d at 751, 37 U.C.C. Rep. Serv. at 1064. Two justices of the Pennsylvania Supreme Court would hold that the acceptance did not meet the offer. The two justices stated, but then ignored the fact, that Litton signed the Bethlehem letter under the words, "Agreed to."

60. Among the terms left open was a mutually agreed-upon index for price escalation "such as" two mentioned indices. At the time of the exercise of the option, an "appropriate clause" was to be included in the contract to provide for quarterly escalations. The terms and specifications, after reference to an attached set, were to contain "any other mutually agreed to terms and conditions" and a clause giving Bethlehem the right to cancel "upon payment of costs." The district judge in the Western District of Pennsylvania was undoubtedly aware of the difficulties price escalation can cause, from that district's experience in *Aluminum Co. of Am. v. Essex Group, Inc.*, 499 F. Supp. 53, 29 U.C.C. Rep. Serv. (Callaghan) 1 (W.D. Pa. 1980) (settled after argument on appeal with an agreed vacation of the order of the district court). The district judge stated that one ground of his decision was that, on the evidence before him, there was no basis on which the missing terms could

cessful, and Bethlehem sued. The proper issue, of course, is whether each party had sufficiently manifested an intent to have an open price contract.

By a four-to-three vote, a seven-judge panel of Pennsylvania's superior court affirmed the no-contract decision of the trial court. The superior court held that the requisite intent to enter into a binding agreement was absent because so many terms were left to future negotiation. In addition, even if the intent could be found, the indefiniteness caused by the number of open terms could not be remedied under U.C.C. section 2-204(3) because there was no reasonably certain basis for filling in those terms consistently with what was expressed to provide an appropriate remedy.<sup>61</sup> The two supreme court justices who voted for affirmance found no contract because "an offer to enter into an option agreement" was not accepted by a letter stating, "we accept the option," even though the purported acceptance was signed "agreed to" by the original offeror. The trial court's finding of a lack of intent to have a contract with open price terms was also affirmed by the two voting for affirmance. Missed was an opportunity to rule that when the manifest intent was not to follow the Code's "gap filler" result, the court should risk that only an "agreement to agree" had been made subject only to an obligation to negotiate in good faith.

## THE BATTLE OF THE FORMS

That U.C.C. section 2-207 was not intended for use when major terms are in dispute is a lesson of *Howard Construction Co. v. Jeff-Cole Quarries, Inc.*,<sup>62</sup> in which the response to the seller's proposal was a purchase order containing considerable price changes. The purchase order was not construed as an expression of acceptance of the proposal. Even if it had been so construed under U.C.C. section 2-305, there was no evidence of an intent to contract with an open price term, and no real basis for a court to fashion a remedy.<sup>63</sup>

Courts continue to require a strict adherence to the Code language that an expression of acceptance, in order not to "operate as an acceptance," must *expressly* make the acceptance conditional on the recipient's *assent* to the additional or different terms.<sup>64</sup>

But subsection 2-207(2)(a) states that terms in a form that contains a definite expression of acceptance do not become part of the contract if "[t]he offer expressly limits acceptance to the terms of the offer." Hence, it is important to determine, when three forms are used, which is the "offer" and which the

be supplied consistently with the expressed intent of the parties. It is unfortunate that the supreme court did not elaborate on this point.

61. 321 Pa. Super. at 371, 468 A.2d at 755, 37 U.C.C. Rep. Serv. at 1069.

62. 669 S.W.2d 221, 37 U.C.C. Rep. Serv. (Callaghan) 1040 (Mo. Ct. App. 1983).

63. As to the statute of frauds, the court said that "[n]one of the writings, whether analyzed separately or in conjunction with each other allows for the inference that an agreement was reached . . ." *Id.* at 230, 37 U.C.C. Rep. Serv. at 1050.

64. *Reaction Molding Technologies, Inc. v. General Elec. Co.*, 588 F. Supp. 1280, 38 U.C.C. Rep. Serv. (Callaghan) 1537 (E.D. Pa. 1984); *Hanford Foundry Co. v. Fuller Co.*, 38 U.C.C. Rep. Serv. (Callaghan) 1553 (E.D. Pa. 1984).

"acceptance." This was done in *Reaction Molding Technologies, Inc. v. General Electric Co.*<sup>65</sup> In that case, RMT submitted numerous quotations to GE. GE then submitted a purchase order to RMT. RMT responded with its own acknowledgment of order form. Both RMT's quotations and acknowledgment of order form contained its standard terms. With its acknowledgment, RMT also objected to GE's delivery term. GE's purchase order contained the following clause: "Acceptance of this order is expressly limited to the conditions of purchase printed on the reverse side."

Relying on a statement by J. White and R. Summers that, generally, the first document to be sent is the offer, the court found that the quotations by RMT were the offers. If the property "is accurately defined and an amount stated as the price in a communication . . . to one person individually," Williston would call it an offer.<sup>66</sup> But when quotations are solicited and submitted, the businessman's conception may be different.<sup>67</sup> It is noteworthy that the clause, which the court ruled did not make the purchase order an acceptance expressly conditioned on assent, is in exact compliance with what U.C.C. section 2-207(2)(a) requires if an *offer* is to nullify the effect of changed terms in an acceptance. It is also questionable that the purchase order contained any "definite and seasonable expression of acceptance." The strictness applied to the wording necessary to comply with the "unless" clause in U.C.C. section 2-207(1) is apparently not to be applied to the determination of whether there is a *definite* and seasonable *expression* of acceptance.

Adopting Summers' view that U.C.C. section 2-207(2) does not apply to *different* terms, the court, because the parties dealt for a while as if a contract existed, moved to U.C.C. section 2-207(3) and cancelled the different terms, which related to delivery and termination. It applied, instead, U.C.C. section 2-309 on delivery and U.C.C. section 2-610 on anticipatory repudiation and entered judgment against GE.

The case illustrates the importance of selecting the form to be characterized as the offer. While the result reflected the intent of the parties, it illustrates a major weakness in the structure of U.C.C. section 2-207 when a counteroffer is intended. The section allows an offeror to submit a form with the qualifying language of U.C.C. section 2-207(2)(a) and increases the likelihood that its terms and conditions will apply to the contract of sale. If this result is not desired, the offeree must always make a counteroffer by using the exact language of the "unless" clause in U.C.C. section 2-207(1), lest it be deemed to have accepted the offeror's provisions. If the offeror uses the "you can accept only on my terms" approach, and the offeree uses the "unless" clause, there will be no contract absent conduct after the exchange of forms. But should such

65. 585 F. Supp. 1097, 38 U.C.C. Rep. Serv. (Callaghan) 1518 (E.D. Pa. 1984).

66. See J. White & R. Summers, *The Uniform Commercial Code* 27 (2d ed. 1980); Williston on Contracts § 27 (3d ed. 1957).

67. Businessmen frequently consider a quotation as no more than an invitation to the recipient to submit an offer, and for that reason neglect to include any number of important terms. See 1 A. Corbin, *Contracts* § 26, at 77 (1963).

conduct trigger U.C.C. section 2-207(3), or should it constitute a traditional common law acceptance of the counteroffer? The Code does not say.

Another troublesome subsection is U.C.C. section 2-207(2)(b), which is applicable if neither party's form uses the appropriate magic qualifying language, both are merchants,<sup>68</sup> and neither reads the other's terms. The issue then boils down to what terms would be "material alterations."

In one case,<sup>69</sup> there was an oral contract followed by a written confirmation signed by both parties containing a disclaimer of warranties. The trial court found the disclaimer ineffective because U.C.C. section 2-207 could not be used to supply the element of explicit negotiation and bargaining required in the state of Washington for an effective disclaimer.<sup>70</sup>

In another case,<sup>71</sup> the Tenth Circuit, applying Kansas law, reversed a trial court's ruling that materiality was an issue of fact. The court also held that defendants were entitled to introduce evidence of a trade usage covering a "replacement or credit" limitation of liability<sup>72</sup> and could use an invoice signed by both parties to impeach the president's testimony that he was not aware of the limitation. The unsigned invoices, the court said, constituted course-of-dealing evidence for the jury to weigh on the issue of express agreement to the limitation of remedy.

Two recent cases have indicated that a forum selection clause<sup>73</sup> and a clause specifying the terms of shipment,<sup>74</sup> as well as warranty and limitation of liability clauses, may be held to be material alterations.

*United States ex rel. United States Steel Corp. v. Construction Aggregates Corp.*<sup>75</sup> involved a double application of U.C.C. section 2-207. An oral contract for the sale of limestone was reached on April 1, 1976, and, thereafter, further documents were exchanged. On April 21, 1976, plaintiff sent a purchase order specifically requiring defendant to supply all the limestone from its primary quarry. Defendant's letter of April 29 stated that it would use its best efforts to supply the limestone from its primary quarry but could not guarantee to do so. The court treated defendant's letter as a U.C.C. section 2-207(2)(c) objection to plaintiff's single-source requirement, thus deleting the additional term. Turning to subsection (2) again, defendant's best efforts clause constituted a "counter

68. *In re Kolob Lumber Co.*, 34 Bankr. 426, 37 U.C.C. Rep. Serv. (Callaghan) 1075 (Bankr. D. Or. 1983).

69. *Rottinghaus v. Howell*, 35 Wash. App. 99, 666 P.2d 899, 37 U.C.C. Rep. Serv. (Callaghan) 42 (1983).

70. *Id.* at 106, 666 P.2d at 903, 37 U.C.C. Rep. Serv. at 47.

71. *Transamerica Oil Corp. v. Lynes, Inc.*, 723 F.2d 758, 37 U.C.C. Rep. Serv. (Callaghan) 1076 (10th Cir. 1983).

72. *Id.* at 765, 37 U.C.C. Rep. Serv. at 1086.

73. *Product Components, Inc. v. Registry Door & Hardware, Inc.*, 568 F. Supp. 651 (S.D. Ind. 1983).

74. *In re Isis Foods, Inc.*, 38 Bankr. 48, 38 U.C.C. Rep. Serv. (Callaghan) 1134 (Bankr. W.D. Mo. 1983).

75. 559 F. Supp. 414 (E.D. Mich. 1983), *aff'd in part and rev'd in part*, 738 F.2d 440 (6th Cir. 1984).

proposal" for an addition to the contract that did not materially alter the contract and thus became a part of it as plaintiff did not object and its purchase order did not contain the qualifying language of U.C.C. section 2-207(2)(a).<sup>76</sup>

## WARRANTIES

### WARRANTY DISCLAIMERS

Even when warranty disclaimer provisions become a part of the parties' agreement, overriding circumstances can limit their applicability. For example, in *Tinker v. De Maria Porsche Audi, Inc.*,<sup>77</sup> warranty disclaimers were held to be ineffective in negating a claim based upon alleged fraudulent representations made by the seller of a second-hand vehicle. The seller had represented that the vehicle was in good operating condition and had not been involved in any major collision. When it was discovered that the car was titled as a "parts car," the purchaser initiated an action based in part upon fraud in the inducement. The trial court entered judgment for the seller notwithstanding the verdict, but the court of appeals reversed, holding that a waiver of oral representations contained in the written sales agreement could not effectively bar claims amounting to fraud in the inducement.<sup>78</sup>

Finally, recent cases have also demonstrated the types of problems that may arise after the sale has been consummated. In *Temple v. Velcro USA, Inc.*,<sup>79</sup> the worst fears of Velcro came to fruition when the plaintiff's husband was killed in the crash of a hot-air balloon that had incorporated a Velcro fastener to secure the deflation panels. Velcro had not been involved in the production of hot-air balloons, and when it discovered that its products were being used for such purposes, it attempted to have the FAA issue an airworthiness directive calling attention to the dangers of such usage. The FAA refused to issue such a directive, and Velcro subsequently mailed a warning to all known registered owners of hot-air balloons using its product that the product should not be used with hot-air balloons. The plaintiff's husband had received the notice and, despite such warnings, continued to use the hot-air balloon. In upholding the summary judgment in favor of Velcro, the court noted that the warning given by Velcro was adequate to defeat claims based on express or implied warranties.<sup>80</sup>

Other postsale actions of the seller with regard to warranty claims can also adversely affect the seller, as was demonstrated in the case of *Oregon Bank v. Nautilus Crane & Equipment Corp.*<sup>81</sup> The court held that, just as the provisions of U.C.C. section 2-316(3)(c) could operate to disclaim an implied warranty, so a course of performance could waive the warranty disclaimers,

76. U.C.C. § 2-207(2)(a) reads: "Between merchants such terms become part of the contract unless: (a) the offer expressly limits acceptance to the terms of the offer."

77. 459 So. 2d 487, 37 U.C.C. Rep. Serv. (Callaghan) 1519 (Fla. Dist. Ct. App. 1984).

78. *Id.* at 492, 37 U.C.C. Rep. Serv. at 1525.

79. 148 Cal. App. 3d 1090, 196 Cal. Rptr. 531, 37 U.C.C. Rep. Serv. (Callaghan) 1108 (1983).

80. The notice was also held effective against strict liability and negligence claims.

81. 68 Or. App. 131, 683 P.2d 95, 38 U.C.C. Rep. Serv. (Callaghan) 1163 (1984).

thereby reinstating the implied warranties of merchantability and fitness for a particular purpose. As a result, summary judgment in favor of the seller was reversed.

The standard warranty waiver provisions found in U.C.C. section 2-316 continue to be limited by consumer-oriented legislation that either amends the section or provides specific consumer protection laws that supersede the section's application. Connecticut has recently modified U.C.C. section 2-316 to prohibit disclaimer of warranties involving sales of new or unused consumer goods unless they are marked "irregular," "factory seconds," or "damaged,"<sup>82</sup> and of all implied warranties. New Hampshire has also amended U.C.C. section 2-316 to prohibit disclaimers on sales of consumer goods by merchants unless a disclaimer that the consumer has signed is given to the consumer.<sup>83</sup> Finally, *Dale v. King Lincoln-Mercury, Inc.*<sup>84</sup> ruled that the Kansas Consumer Protection Act<sup>85</sup> prevents an express warranty contained in the sales contract from limiting the implied warranty of merchantability in cases involving consumer goods.

## WARRANTY BENEFICIARIES

The three alternatives of U.C.C. section 2-318 inserted in 1956 affected only horizontal privity. The majority of the states adopted Alternative A, which covers only the "family or household" of the buyer and is limited to personal injuries. In *Boddie v. Litton Unit Handling Systems*,<sup>86</sup> an Illinois appellate court refused to extend privity to employees of the U.S. Postal Office despite a judicially created "family" relationship between a corporation and its employees.<sup>87</sup> Similarly, in *Professional Lens Plan, Inc. v. Polaris Leasing Corp.*,<sup>88</sup> the Kansas Supreme Court held that under Alternative A a corporate plaintiff suing for lost profits and other economic loss was not injured in person "and so not a third party beneficiary" of the impleaded manufacturer's warranties.

An interesting distinction appears in *N. Feldman & Son v. Checker Motors Corp.*<sup>89</sup> In that case, defendant General Motors Corp., a seller of diesel engines

82. Conn. Gen. Stat. § 42a-2-316 (1984).

83. N.H. Rev. Stat. Ann. § 38-A:2-316(4) (1961 & Supp. 1983).

84. 234 Kan. 840, 676 P.2d 744, 38 U.C.C. Rep. Serv. (Callaghan) 35 (1984).

85. Kan. Stat. Ann. § 50-639 (1980).

86. 118 Ill. App. 3d 520, 455 N.E.2d 142, 37 U.C.C. Rep. Serv. (Callaghan) 1116 (1983). Alternatively, the court held that they were not employees of the subcontractor purchaser of the conveyor belt system installed in the post office. Cf. *Nebraska Innkeepers, Inc. v. Pittsburgh-Des Moines Corp.*, 345 N.W.2d 124, 38 U.C.C. Rep. Serv. (Callaghan) 1177 (Iowa 1984) (economic loss not recoverable as warranty beneficiaries by retail stores losing trade because of defective steel in a bridge); *Pronti v. DML of Elmira, Inc.*, 478 N.Y.S.2d 156, 39 U.C.C. Rep. Serv. (Callaghan) 455 (App. Div. 1984) (no implied warranty from a manufacturer to a subpurchaser when no personal injury involved).

87. Cf. *Delta Oxygen Co. v. Scott*, 238 Ark. 534, 383 S.W.2d 885, 2 U.C.C. Rep. Serv. (Callaghan) 388 (1964); *Barfield v. Atlantic Coast Line R.R.*, 197 So. 2d 545 (Fla. Dist. Ct. App. 1967); *Salvador v. Atlantic Steel Boiler Co.*, 459 Pa. 24, 319 A.2d 903, 14 U.C.C. Rep. Serv. (Callaghan) 1073 (1974).

88. 234 Kan. 742, 675 P.2d 887, 38 U.C.C. Rep. Serv. (Callaghan) 69 (1984).

89. 572 F. Supp. 310, 37 U.C.C. Rep. Serv. (Callaghan) 730 (S.D.N.Y. 1983).



to Checker, moved for summary judgment. Applying Michigan law, the court denied General Motors' motion with respect to the express warranty count but granted the motion with respect to the implied warranty of merchantability count. Under Michigan's version of sections 2-314 and 2-318 of the Code, implied warranties extend only to the family or household of the immediate buyer, who cannot recover for economic loss. However, specific representations do extend to a remote buyer if proved to be a part of the basis of the bargain, and economic loss is then recoverable.

Florida's privity rule was considered by a panel of its Third District Court of Appeal in *GAF Corp. v. Zack Co.*<sup>90</sup> Recovery against a seller once removed from plaintiff purchaser was denied. In a second case, *Cedars of Lebanon Hospital Corp. v. European X-Ray Distributors of America, Inc.*,<sup>91</sup> another panel (on which sat one judge from the *GAF* case) traced the erosion, in both Florida and general law, of the privity requirement. In the absence of a clear statement by the Florida legislature that its version of U.C.C. section 2-318 was intended to abrogate all of Florida's pre-Code exceptions to privity, the court applied one to permit recovery against the remote manufacturer that had made direct representations to the hospital to induce it to buy x-ray equipment from a distributor. A footnote to the opinion emphasizes that the decision rests on direct contact between the manufacturer and the ultimate purchaser; absent direct contact, lack of privity would, it said, still defeat recovery.<sup>92</sup>

### **TITLE, CREDITORS, AND GOOD FAITH PURCHASERS**

In *Monsanto Co. v. Walter E. Heller & Co.*,<sup>93</sup> the court held that Heller was not a good faith buyer obtaining a better title than its transferor because Heller knew that its debtor was buying on credit, had an understanding with the credit seller that Heller would advance sufficient funds to pay for the purchases, and had given the credit seller reason to rely on the continuation of that practice. The opinion underscores the rule that in connection with merchants, at least in article 2 cases, a higher standard of good faith is required than for non-merchants.

The prior owner's attempt to recover failed in *Brumley Estate v. Iowa Beef Processors, Inc.*<sup>94</sup> The Fifth Circuit decided that the cash sale rule, when the seller was not paid, did not result, as some cases have held, in a void transaction, but in a transaction void only as between the parties, which did not negate the title of a good faith purchaser from the nonpaying buyer.<sup>95</sup> In *Shell Oil Co. v. Mills Oil Co.*,<sup>96</sup> the unpaid credit seller contended that a bank with an inventory

90. 445 So. 2d 350, 37 U.C.C. Rep. Serv. (Callaghan) 1113 (Fla. Dist. Ct. App. 1984).

91. 444 So. 2d 1068, 38 U.C.C. Rep. Serv. (Callaghan) 40 (Fla. Dist. Ct. App. 1984).

92. *Id.* at 1072 n.4, 38 U.C.C. Rep. Serv. at 47 n.5.

93. 114 Ill. App. 3d 1078, 449 N.E.2d 993, 36 U.C.C. Rep. Serv. (Callaghan) 834 (1983).

94. 704 F.2d 1351, 36 U.C.C. Rep. Serv. (Callaghan) 819 (5th Cir.), *modified*, 715 F.2d 996 (5th Cir. 1983), *cert. denied*, 104 S. Ct. 1288 (1984).

95. 704 F.2d at 1362, 36 U.C.C. Rep. Serv. at 826.

96. 717 F.2d 208, 37 U.C.C. Rep. Serv. (Callaghan) 116 (5th Cir. 1983).

lien was not a bona fide purchaser because it had in the past honored the credit buyer's drafts, even if overdrafts, and had not informed the credit seller that it was refusing further credit to the buyer. The court held that a greater connection with the wrongful activities of the buyer was needed in order to find a triable issue as to lack of good faith.

An attempt to defeat the application of U.C.C. section 2-326 by implying that the consignee must be a seller of the consignor's goods, even though a seller of similar goods, failed in a Florida appeals court case,<sup>97</sup> and creditors of the consignee prevailed. The goods were delivered to the operator of a warehouse facility under a contract using the term "consigned," providing for the passage of risk of loss upon delivery to the warehouse, and requiring the warehouse operator to assist the owner of the goods "in any reasonable manner to protect the interest of Defendant [owner] 'in this consignment transaction including, but not limited to, execution [of] financing statement, posting of signs under a sign law, and otherwise.'"<sup>98</sup> No such action was taken. Sales were made and invoices sent only by the owner. The warehouse operator had no authority to sell, but when delivery was accomplished the operator did notify the owner and did receive an eight percent commission on the sales. The warehouse operator conducted a sales business for similar items on its premises and under its own name. In *Simonds-Shields-Theis Grain Co. v. Far-Mar-Co.*,<sup>99</sup> SST hired a trucker known to it to be a "sometime" dealer in soybeans to deliver beans under a contract it had with FMC. When delivering the grain, the trucker represented it as his own and was paid. SST's conversion action against the buyer from the trucker was defeated. The Fifth Circuit ruled that the policy of U.C.C. sections 2-403(2) and (3) extends to one engaged in "occasional merchandising." Recovery was also defeated on common law agency and estoppel principles.<sup>100</sup>

## **TENDER, CURE, AND NOTICE OF BREACH**

U.C.C. section 2-602 allows for rejection of goods "within a reasonable time after their delivery." During discussion of "overheating," when a new truck with a snowplow attachment was tested, the buyer was told that readjustment of

97. *Georgia-Pacific Corp. v. Walter E. Heller & Co.*, 440 So. 2d 666, 37 U.C.C. Rep. Serv. (Callaghan) 735 (Fla. Dist. Ct. App. 1983).

98. *Id.* at 667, 37 U.C.C. Rep. Serv. at 737.

99. 575 F. Supp. 290, 37 U.C.C. Rep. Serv. (Callaghan) 1547 (W.D. Mo. 1983).

100. The court said:

A Fifth Circuit decision notes that "the phrase 'or had power to transfer' in section 2-403(1) makes clear that common-law concepts of agency and estoppel (based on actual or apparent authority) may be invoked by a party who purchases goods from an agent or apparent agent of the true owner."

*Id.* at 293, 37 U.C.C. Rep. Serv. at 1551 (quoting *American Standard Credit, Inc. v. National Cement Co.*, 643 F.2d 248, 266 (5th Cir. 1981)).

the position of the blade would cure the problem.<sup>101</sup> Sale papers were signed, and a full payment check was given. But the overheating continued and was not cured. The buyer immediately notified the seller that it was not taking the truck, told the seller it was stopping payment on the check (it did so), and told the seller to repossess the truck.

Instead, claiming acceptance by the buyer, seller processed the title papers, and title was duly issued in buyer's name. The court held that the case was one of rejection, that "[a] 'reasonable time to inspect' under the UCC must allow an opportunity to put the product to its intended use, or for testing to verify its capability to perform as intended."<sup>102</sup> The notice given was sufficient because it indicated the relief wanted and was timely for the purpose.

The conflict between two sentences in comment 4 to U.C.C. section 2-607 regarding the required content of notice continues to cause trouble.<sup>103</sup> One group of cases relating to warranties follows the "still troublesome" first sentence.<sup>104</sup> Another group follows the "claimed to involve a breach" rule of the last sentence.<sup>105</sup>

Without regard to the slightly different language regarding notice in U.C.C. section 2-608(2), cases frequently use the same tripartite statement of the purposes of notice<sup>106</sup> found in comment 5 to this section, perhaps because it seems to imply that the purposes are the same.

As to the timing of the notice, there are examples of a division between cases treating the notice as a "condition precedent to suit" in order to afford time for

101. *Capitol Dodge Sales, Inc. v. Northern Concrete Pipe, Inc.*, 38 U.C.C. Rep. Serv. (Callaghan) 114 (1983).

102. *Id.* at 119.

103. The first sentence of the second paragraph of comment 4 reads: "The content of notification need merely be sufficient to let the seller know that the transaction is still troublesome and must be watched." The last sentence states: "The notification which saves the buyer's rights under this Article need only be such as informs the seller that the transaction is claimed to involve a breach, and thus opens the way for normal settlement through negotiation."

104. *Royal Typewriter Co. v. Xerographic Supplies Corp.*, 719 F.2d 1092, 37 U.C.C. Rep. Serv. (Callaghan) 429 (11th Cir. 1983); *International Technical Instruments, Inc. v. Engineering Measurements Co.*, 678 P.2d 558, 38 U.C.C. Rep. Serv. (Callaghan) 868 (Colo. Ct. App. 1983).

105. *Speakman Co. v. Harper Buffing Mach. Co.*, 583 F. Supp. 273, 38 U.C.C. Rep. Serv. (Callaghan) 469 (D. Del. 1984); *Barrington Corp. v. Patrick Lumber Co.*, 447 So. 2d 785, 38 U.C.C. Rep. Serv. (Callaghan) 744 (Ala. Civ. App. 1984); *Agway, Inc. v. Teitscheid*, 144 Vt. 76, 472 A.2d 1250, 38 U.C.C. Rep. Serv. (Callaghan) 818 (1984).

106. Comment 5 indicates that the "purposes" of the requirement of notice are "considerations of good faith, prevention of surprise, and reasonable adjustment." It has been said that these purposes are met if the notice informs the seller that the buyer has revoked, giving identification of the particular goods he has revoked and setting forth the nature of the nonconformity. *Solar Kinetics Corp. v. Joseph T. Ryerson & Son, Inc.*, 488 F. Supp. 1237, 29 U.C.C. Rep. Serv. (Callaghan) 85 (D. Conn. 1980).

settlement<sup>107</sup> and those holding that a timely filing of suit satisfies the notice requirement.<sup>108</sup>

*Smith v. Stewart*<sup>109</sup> involved the purchase of a yacht. Neither party was a merchant, but the seller gave an express warranty against any dry rot discovered within six months. Three days after delivery of the boat, the buyer notified the seller of a fuel tank leak and requested defrayal of the expense of repairing the tank. In the ensuing discussions, congeniality turned to hostility, and both parties retained attorneys. A few days before the end of the six-month period, dry rot was discovered, but the seller was not notified. About three weeks later, buyer filed suit for both the fuel tank repairs and the dry rot. The trial court entered summary judgment for seller on all claims because there was no implied warranty of merchantability since the seller was not a "boat-merchant," and also because buyer had given no notice of breach regarding the dry rot.

The Kansas Supreme Court, on appeal, affirmed as to the fuel tank leak and reversed as to the dry rot. Adopting the White and Summers view of the purposes behind the notice requirement,<sup>110</sup> the court had to face the extensive case law and scholarly comment supporting the condition precedent approach with its personal injury relaxation<sup>111</sup> and its third-party beneficiary exception.<sup>112</sup> Without expressly creating an "already in a hostile position" exception to the notice rules as such, the court held that filing suit constituted sufficient notice in this case.

In *Shooshanian v. Wagner*,<sup>113</sup> the Alaska Supreme Court said in a consumer breach of warranty suit, "The filing of a complaint is certainly not a bar to the negotiation and settlement of claims. To the contrary, the prospect of going to trial is often a powerful incentive to a defendant to investigate the claims against it and to arrive at a reasonable agreement."<sup>114</sup> The court, in reversing an order dismissing a complaint with prejudice, also said that a defendant could more easily prepare for either settlement or trial through the use of pretrial discovery techniques. The court added that "[a]llowing a consumer's complaint to serve as notice will not prevent a defendant manufacturer from raising the issue of timeliness if it has been prejudiced by an unreasonable delay."<sup>115</sup>

107. The court in *Smith v. Stewart*, 233 Kan. 904, 667 P.2d 358, 36 U.C.C. Rep. Serv. (Callaghan) 1141 (1983), was generally supportive of this view.

108. *Owens v. Glendale Optical Co.*, 590 F. Supp. 32, 39 U.C.C. Rep. Serv. (Callaghan) 903 (S.D. Ill. 1984); *Palmer v. A.H. Robins Co.*, 38 U.C.C. Rep. Serv. (Callaghan) 1150 (Colo. 1984).

109. 233 Kan. 904, 667 P.2d 358, 36 U.C.C. Rep. Serv. (Callaghan) 1141 (1983).

110. See J. White & R. Summers, *supra* note 66, § 11-10.

111. See generally *id.*

112. *Id.*

113. 672 P.2d 455, 37 U.C.C. Rep. Serv. (Callaghan) 55 (Alaska 1983).

114. *Id.* at 462-63, 37 U.C.C. Rep. Serv. at 59.

115. *Id.* at 463, 37 U.C.C. Rep. Serv. at 59-60.

A notice once given may have to be renewed if buyer's intervening conduct lulls a reasonable seller into believing that the defect has been cured or has disappeared.<sup>116</sup>

The intermesh of a buyer's right to revoke acceptance and a seller's right to cure by replacement rather than repair was before the Texas Supreme Court in *Gappelberg v. Landrum*.<sup>117</sup> The intermediate appellate court, reversing the trial court, had distinguished cases denying the right to cure on the ground that they involved only the right to cure by repair. It held that the "spirit of the Code" required the allowance of cure by complete replacement. The supreme court reversed, citing *Zabriskie Chevrolet Inc. v. Smith*<sup>118</sup> for its theory of "shaken faith" in a product, in this case a large-screen television, that had an undiscovered substantial defect when accepted.

## REPUDIATION AND EXCUSE

The demand for assurances provision, U.C.C. section 2-609, was considered in *Clem Perrin Marine Towing, Inc. v. Panama Canal Co.*<sup>119</sup> The Canal Company had chartered a tug with an option to purchase. Nineteen days before the final charter payment was due, the Canal Company wrote the owner that it had discovered that one of the mortgages on the tug was in default and demanded assurances that clear title to the tug would be available on or before the date for the exercise of the option. It stated that it was withholding payments until it received assurances and did so. No answer was given except by a suit, filed two days after the due date of the payment, for the return of the boat. The district court gave judgment to the now-bankrupt plaintiff.

The Fifth Circuit reversed, holding that the U.C.C. governed the contract for sale under federal law, whether common law or admiralty. The owner claimed that, under U.C.C. section 2-609, withholding payment was not "commercially reasonable" as the Canal Company had made no investigation of the owner's financial condition and payments on the mortgages could obviously be made from the lease rentals.<sup>120</sup> The court held that if the owner was in fine financial shape, all it had to do in response to the request for assurances "was to explain the situation." The standard for demanding assurances is "one of reasonable insecurity, not absolute certainty."<sup>121</sup> The withholding of payment (suspension of performance) was reasonable when the request for assurances was greeted by absolute silence.

116. *Agway, Inc. v. Teitscheid*, 144 Vt. 76, 472 A.2d 1250, 38 U.C.C. Rep. Serv. (Callaghan) 818 (1984).

117. 666 S.W.2d 88, 37 U.C.C. Rep. Serv. (Callaghan) 1563 (Tex. 1984).

118. 99 N.J. Super. 441, 240 A.2d 195, 5 U.C.C. Rep. Serv. (Callaghan) 30 (1968).

119. 730 F.2d 186, 38 U.C.C. Rep. Serv. (Callaghan) 490 (5th Cir. 1984).

120. *Id.* at 190, 38 U.C.C. Rep. Serv. at 496.

121. *Id.* at 191, 38 U.C.C. Rep. Serv. at 497.

*Consolidated Edison Co. v. Charles F. Guyon, Inc.*<sup>122</sup> shows that the party giving assurances can go too far. Defendant had contracted to supply a quantity of fabricated piping but thereafter decided to shut down its fabricating division. Consolidated Edison asked for a confirmation in nine days that the pipe would still be supplied. U.C.C. section 2-609 provides that the demand for assurances must be in writing but says nothing about how the assurances should be given. Summary judgment on liability issues was granted, as the proffered oral "assurances" were that defendant would place the order with another supplier if Consolidated Edison would look solely to that supplier with respect to any product liability for unfinished merchandise.<sup>123</sup> A proffered novation does not constitute assurances.

The doctrine of impracticability of performance resulted in a reversal of a \$5 million judgment due to improper jury instructions that, in effect, constituted directed verdicts on certain issues in *Zidell Explorations, Inc. v. Conval International, Ltd.*<sup>124</sup> The case arose from a termination of plaintiff's distributorship of valves imported by Conval. Defendant did not fill two orders placed before termination and urged impracticability as an excuse.

The Ninth Circuit construed the contract as one to supply from an agreed source, since prices were tied to prices charged defendant by a specified Yugoslavian company. The court then ruled that the failure to supply by the agreed source would constitute impracticability only if defendant had used all due measures to assure that its supplier would perform, and the evidence on that issue raised a jury question.

The second and more interesting aspect was the failure of Conval to assign to Zidell all of Conval's rights against the supplier. Despite the comment's statement that a condition of "making good the claim of excuse" is the assignment, the court declined to make the failure to assign a per se invalidation of the impracticability excuse. The jury should decide, it ruled, whether in view of all the circumstances there was any breach of good faith in failing to assign the rights.

The gyrations in the world oil market in 1979 and thereafter have produced at least three resorts to U.C.C. section 2-615, of which two will be discussed. In *Interpetrol Bermuda Ltd. v. Kaiser Aluminum International Corp.*,<sup>125</sup> a contract for petroleum to be refined in Taiwan was involved. The contract contained a force majeure clause, which excused a performance if the specified events occurred before departure of the vessel from a loading port in the Persian Gulf.

A Ninth Circuit panel affirmed the district court's holding that the force majeure clause excused the seller if its supplier failed to supply "for any reason whatsoever, as long as the vessel had not been loaded." The circuit court then ruled that U.C.C. section 2-615 had no application as the events that occurred

122. 98 A.D.2d 483, 471 N.Y.S.2d 269, 37 U.C.C. Rep. Serv. (Callaghan) 1132 (App. Div. 1984).

123. *Id.* at 484-85, 471 N.Y.S.2d at 270, 37 U.C.C. Rep. Serv. at 1132-33.

124. 719 F.2d 1465, 37 U.C.C. Rep. Serv. (Callaghan) 466 (9th Cir. 1983).

125. 719 F.2d 992, 37 U.C.C. Rep. Serv. (Callaghan) 779 (9th Cir. 1983).

were foreseeable and the clause represented the parties' bargain as to who should bear the loss.<sup>126</sup> The panel then held that the covenant of good faith, which the California courts had read into force majeure clauses, does not include the obligation to allow the buyer to succeed to the excused seller's rights against its supplier. The windfall of any such recovery, based on the absence of any excusing clause in seller's contract with its supplier, belonged to the seller by reason of its superior bargaining.

In *Nissho-Iwai Co. v. Occidental Crude Sales, Inc.*,<sup>127</sup> a jury awarded Nissho damages for Occidental's failure to deliver oil from Libya. Occidental urged as excuses an embargo by the Libyan government and pipeline breakdowns. The trial judge instructed the jury that it must find that the excusing event or events were not reasonably within the control of Occidental or its supplier. The Fifth Circuit held the instruction to be proper. The concept of an American jury determining whether Occidental provoked Colonel Khadafy's actions or whether his actions were beyond its reasonable control raises interesting speculations.

## REMEDIES

### REJECTION AND REVOCATION OF ACCEPTANCE

In *Bowlin's Inc. v. Ramsay Oil Co.*,<sup>128</sup> the New Mexico Court of Appeals upheld a contractual two-day clause for objection to deliveries of gasoline to service stations. The claim of an unconscionably short time was defeated by a showing that the purchaser's "Procedures for Verifying the Quantity of Gasoline Delivered to Your Store," if followed, would have enabled each outlet to verify quantities within hours after delivery.<sup>129</sup>

At the other end of the spectrum is *Sumner v. Fel-Air, Inc.*,<sup>130</sup> in which repeated assurances that a substantial defect would be cured worked to extend the period for revocation of acceptance.

The "reasonable" time for rejection was extended in *In re H.P. Tool Manufacturing Corp.*<sup>131</sup> In order for inspection to be made, the seller would have had to depart from normal procedures, open each carton of tool sets, and unroll the pouches. Hence, notice given after receipt of complaints from customers was timely and effective to revoke acceptance. The resales did not constitute an improper exercise of dominion.

On the other hand, shoes are different from tool sets. In *Lorenzo Banfi di Banfi Renzo & Co. v. Davis Congress Shops, Inc.*,<sup>132</sup> rejection failed when delivery was taken in early summer 1982 and notice of nonconformity was given

126. *Id.* at 999, 37 U.C.C. Rep. Serv. at 788.

127. 729 F.2d 1530, 38 U.C.C. Rep. Serv. (Callaghan) 1237 (5th Cir. 1984).

128. 99 N.M. 660, 662 P.2d 661, 36 U.C.C. Rep. Serv. (Callaghan) 1110 (N.M. Ct. App. 1983).

129. *Id.* at —, 662 P.2d at 670, 36 U.C.C. Rep. Serv. at 1122.

130. 680 P.2d 1109, 38 U.C.C. Rep. Serv. (Callaghan) 91 (Alaska 1984).

131. 37 Bankr. 885, 38 U.C.C. Rep. Serv. (Callaghan) 110 (Bankr. E.D. Pa. 1984).

132. 568 F. Supp. 432, 36 U.C.C. Rep. Serv. (Callaghan) 1183 (N.D. Ill. 1983).

in mid-August, but the shoes were continuously offered for sale and half had been sold by April 1983.

## RECLAMATION

In *Myers v. Columbus Sales Pavilion, Inc.*,<sup>133</sup> an unpaid cash seller sued the buyer's auctioneer. The district court, affirmed by the Eighth Circuit on the basis of the district court's opinion by Judge Urbom, ruled that under U.C.C. section 2-507(2), title passed from seller to buyer, and that U.C.C. section 2-401(4) is an exclusive listing of the circumstances in which title, having passed, is vested in a seller. U.C.C. section 2-507(2) was said to speak only of the buyer's right, as against the seller, to retain or dispose of the purchased cattle,<sup>134</sup> not of a revesting of title. Hence, the rights of third parties were not affected and the auctioneer committed no conversion, as the seller had no property interest in the cattle.

A better approach would have applied the "innocent agent" rule to the auctioneer<sup>135</sup> or have equated the position of the auctioneer to that of a good faith purchaser.

Finally, the district court judge, Judge Urbom, had applied the Nebraska statute<sup>136</sup> relieving an auctioneer of liability for conversion when selling personal property at auction in good faith and without notice of a security interest, provided that the principal is disclosed and the auctioneer has no interest in the property except to act as an intermediary. The Eighth Circuit, however, affirmed only the U.C.C. analysis leading to "no conversion." It then stated that the portion of Judge Urbom's opinion considering the Nebraska statute "is to be regarded as surplusage, and we express no view thereon."<sup>137</sup>

The Tenth Circuit considered the effect of Kansas law on a secured party dealing with a nonpaying buyer when reclamation was sought under U.C.C. section 2-507(2).<sup>138</sup> It held that the return of the buyer's check defeated the buyer's title, so that it never had rights in the purchased goods to support the grant of a security interest. It then went on to rule, however, that because the seller failed to pursue its right to reclaim diligently, the sale was no longer conditional and the buyer could sell or give a security interest.

Unfortunately for the Tenth Circuit, the Kansas Supreme Court reached the opposite result three months later in *Iola State Bank v. Bolan*.<sup>139</sup> Involved were

133. 575 F. Supp. 805, 37 U.C.C. Rep. Serv. (Callaghan) 1122 (D. Neb.), *aff'd*, 723 F.2d 37, 37 U.C.C. Rep. Serv. (Callaghan) 1128 (8th Cir. 1983).

134. 575 F. Supp. at 808, 37 U.C.C. Rep. Serv. at 1125. District Judge Urbom ruled that plaintiff could not recover in conversion as title had passed from plaintiff and U.C.C. § 2-507 did not provide the unpaid seller even a security interest. *Id.*, 37 U.C.C. Rep. Serv. at 1125.

135. Compare the position of a selling agent or broker under U.C.C. §§ 3-417(4) and 3-419(3). Compare also U.C.C. §§ 2-312(2) and 2-328(4), referring to auctioneer's principal as "the seller."

136. Neb. Rev. Stat. § 69-109.01 (Reissue 1981).

137. 723 F.2d at 38, 37 U.C.C. Rep. Serv. at 1130.

138. *Holiday Rambler Corp. v. First Nat'l Bank & Trust Co.*, 723 F.2d 1449, 37 U.C.C. Rep. Serv. (Callaghan) 1553 (10th Cir. 1983).

139. 235 Kan. 175, 679 P.2d 720, 38 U.C.C. Rep. Serv. (Callaghan) 755 (1984).



farmer sellers of grain, a merchant buyer, and the after-acquired property clause of the bank's security agreement with the buyer. The court considered that the Code radically changed the Kansas pre-Code "cash sale" rule from "void" to "voidable." Thus, unpaid sellers in Kansas were now subject to the claims of good faith purchasers from the nonpaying buyer. Unfortunately for it, the bank that dishonored the checks was the same bank that claimed purchaser status under its security agreement. The bank was found to have knowledge that the funds in the account belonged to the farmers, so that its setoff of the buyer's balance was distinctly not in good faith. The trial court's direction of a verdict in favor of the farmers for both compensatory damages and \$150,000 in punitive damages was sustained.

While the issue of good faith was not considered by the trial court or jury, the appellate court ruled that the trial judge's findings made clear that the bank had not acted honestly in fact; hence, as a matter of law, the bank was not a good faith purchaser<sup>140</sup> and so had converted the farmers' money, a tort allowing recovery of punitive damages.

The issue whether a secured party, claiming as a good faith purchaser, must have advanced money after the goods were delivered, possibly implicit in the two preceding cases, was thought by many to have been put to rest by *In re Samuels & Co.*<sup>141</sup> Possibly emboldened by the rash of contrary statutes and the federal enactment following that case,<sup>142</sup> Bankruptcy Judge Emil F. Goldhaber, departing from the views of many of his colleagues,<sup>143</sup> ruled in *Lavonia Manufacturing Corp. v. Emery Corp. (In re Emery Corp.)*<sup>144</sup> that a secured party, to prevail over the reclaiming seller under U.C.C. section 2-702(3), must "take" the interest by giving value during the period after receipt of the goods and before the reclamation demand is made.<sup>145</sup>

140. *Id.* at \_\_\_\_, 679 P.2d at 730-31, 38 U.C.C. Rep. Serv. at 767. Because a directed verdict was the correct result even though the trial court's reasoning was not applicable, the court ruled that the verdict should stand. *Id.* at \_\_\_\_, 679 P.2d at 731, 38 U.C.C. Rep. Serv. at 767-68. The court also ruled that the bank, because of its knowledge, had no common law or statutory right of setoff against the farmers' funds. *Id.* at \_\_\_\_, 679 P.2d at 733-34, 38 U.C.C. Rep. Serv. at 772.

141. 526 F.2d 1238, 18 U.C.C. Rep. Serv. (Callaghan) 545 (5th Cir.), *cert. denied*, 429 U.S. 834 (1976). The Kansas court cites 10 other opinions reaching the same result.

142. The initial adverse reaction to *Samuels* can be seen in Okla. Stat. Ann. tit. 2, §§ 9-138, -139 (West Supp. 1984-1985); 3A Kan. Stat. Ann. §§ 47-1801, -1802 (1981); Ten. Civ. Code Ann. tit. 121, art. 6910(b) (Vernon 1960), *repealed* in 1981 (Vernon Supp. 1985); 1976 Cal. Stat. 772 (Assembly Bill 3485). Then came the federal statute, Pub. L. No. 94-410, 90 Stat. 1249 (Sept. 13, 1976), *explained* in H.R. Rep. No. 94-1043 (Apr. 14, 1976).

143. See, for example, Judge Goldhaber's footnotes 9 and 10. *Lavonia Mfg. Corp. v. Emery Corp. (In re Emery Corp.)*, 38 Bankr. 489, 495, 38 U.C.C. Rep. Serv. (Callaghan) 834, at 842-43 (Bankr. E. D. Pa. 1984).

144. 38 Bankr. 489, 38 U.C.C. Rep. Serv. (Callaghan) 834 (Bankr. E.D. Pa. 1984). *Contra In re Bensar Co.*, 36 Bankr. 699, 38 U.C.C. Rep. Serv. (Callaghan) 823 (Bankr. S.D. Ohio 1984).

145. The judge posed two alternatives: first, that the U.C.C. displaced state common law and that rights of creditors must be found under article 2 (Pennsylvania has the 1966 amendment to U.C.C. § 2-702); and second, state law has not been displaced. Under Pennsylvania law, *Mann v. Salsberg*, 17 Pa. Super. 280 (1901), and *In re Kravitz*, 278 F.2d 820, 1 U.C.C. Rep. Serv. (Callaghan) 159 (3d Cir. 1960), the judge concluded that only a "reliance interest" is protected. He

If electronic means are used to transmit the demand for reclamation, when is the demand made? *Montello Oil Corp. v. Marin Motor Oil, Inc. (In re Marin Motor Oil Co.)*<sup>146</sup> involved a last day for demand on April 21, 1981. At 11:04 p.m. that day, a telex was sent to the buyer and was received by Western Union's office serving the buyer at 11:08 p.m. The message was not in readable form until the buyer opened for business and turned on its machine at 9:04 a.m. on April 22, 1981. The Third Circuit panel adopted a "dispatch" rule for the timeliness of demands. Factors justifying its decision were said to be the difficulty of proof of receipt, the uncertainty of proving just where the message was between 11:08 p.m. and 9:04 a.m. the next day, and the lack of any guiding policy as to the purpose of a demand. The policy selected was that of favoring certainty in the law. The opinion states that under a dispatch rule the method of communication chosen by the seller must be commercially reasonable in the light of past practices between the parties and in the industry.<sup>147</sup>

### BUYER'S MONEY REMEDIES; LIMITATIONS ON REMEDIES AND DAMAGES

Although comment 2 to U.C.C. section 2-715 explicitly rejects the "tacit agreement" test, defendants persistently argue that consequential damages are recoverable only if they were *contemplated* at the time of contracting. Courts continue to reject the argument.<sup>148</sup>

In *McGinnis v. Wentworth Chevrolet Co.*,<sup>149</sup> the Oregon Supreme Court reversed the intermediate appellate court's allowance, to a buyer revoking acceptance, of the cost of renting a substitute automobile as "cover," and remanded to determine if recovery could be had as consequential damages. It is clear, however, that the rental was neither cover nor "incidental damages" and could be recovered, if at all, only as consequential damages, subject to the validity of a clause in the contract excluding consequential damages.

The remand will require Oregon to take a position on whether a revocation of acceptance, when a repair or replacement limited remedy fails of its essential

analyzed U.C.C. § 2-702 to indicate that divestiture of the right to reclaim must be triggered by an action of the purchaser or buyer in ordinary course occurring after delivery and before demand is made. There are those on the subcommittee who believe that the judge is in error.

146. 740 F.2d 220, 38 U.C.C. Rep. Serv. (Callaghan) 1425 (3d Cir. 1984).

147. The case also involved an issue as to the date the goods were "received" by the buyer. The court applied U.C.C. § 2-103(1)(c)'s definition of receipt, not as controlling state law, but as a rule suitable for federal purposes. Thus, goods were not "received" while in the possession of a common carrier, even one selected by the buyer. The seller's right of stoppage in transitu under U.C.C. § 2-705 indicated that the buyer did not have unfettered possession; hence, there was no receipt until delivery to a bailee acting exclusively for the buyer. *Id.* at 224-25, 38 U.C.C. Rep. Serv. at 1432-33.

148. *See, e.g., Elar Invs., Inc. v. Southwest Culvert Co.*, 139 Ariz. 25, 28, 676 P.2d 659, 662, 38 U.C.C. Rep. Serv. (Callaghan) 138, 141 (1983).

149. 295 Or. 494, 668 P.2d 365, 37 U.C.C. Rep. Serv. (Callaghan) 130 (1983) (en banc).

purpose, also defeats the contractual exclusion of consequential damages.<sup>150</sup> Attacks on such exclusion clauses as "unconscionable" continue to fail in a commercial context.<sup>151</sup>

*Barnard v. Compugraphic Corp.*<sup>152</sup> joins with the cases holding that interest on money borrowed to make a purchase is not recoverable when the buyer is awarded lump sum damages. The rationale is that the awarded damages permit a replacement purchase to be made without additional borrowing. But the extended time factor where interest is paid without obtaining the benefit of use of the product is ignored. On the other hand, interest on money borrowed to make repairs because of defendant's breach qualifies as consequential damages.<sup>153</sup> But for the breach, the money would not have been borrowed.

In *Nezperce Storage Co. v. Zenner*,<sup>154</sup> Nezperce bought wheat from Zenner, who expressly warranted it to be spring wheat. Zenner knew that Nezperce would process the grain into spring wheat seed and then resell it. Under their contract, Zenner was obliged to indemnify Nezperce for losses suffered upon resale. When the seed proved defective, Nezperce felt it was forced to settle with its buyers. As the jury found that the settlement amounts were reasonable, the court allowed their recovery as consequential damages. Without a finding that the settlements were reasonable, recovery would ordinarily be denied. An indemnity against loss ordinarily does not grant checking privileges on the indemnitor.

## **STATUTES OF LIMITATIONS—INTERACTION OF TORT, CONTRACT, AND PRODUCT LIABILITY STATUTES**

In view of the difficulty of distinguishing causes of action in contract from those in tort, the four-year statute of limitations contained in U.C.C. section 2-725 continues to spawn conflicting decisions. When the defect resulted solely in economic loss, most courts thought U.C.C. section 2-725 governed,<sup>155</sup> even to the

150. Leary & Frisch, *Uniform Commercial Code Annual Survey: General Provisions, Sales, Bulk Transfers, and Documents of Title*, 39 Bus. Law. 1851, 1897 (1984) (discussing the existing division of opinion).

151. *Transamerica Oil Corp. v. Lynes, Inc.*, 723 F.2d 758, 37 U.C.C. Rep. Serv. (Callaghan) 1076 (10th Cir. 1983); *Frantz Lithographic Serv., Inc. v. Sun Chem. Corp.*, 38 U.C.C. Rep. Serv. (Callaghan) 485 (E.D. Pa. 1984); *In re Feder Litho-Graphic Servs., Inc.*, 40 Bankr. 486, 39 U.C.C. Rep. Serv. (Callaghan) 495 (Bankr. E.D. Mich. 1984).

152. 35 Wash. App. 414, 667 P.2d 117, 37 U.C.C. Rep. Serv. (Callaghan) 141 (1983).

153. *Metropolitan Transfer Station, Inc. v. Design Structures, Inc.*, 328 N.W.2d 532, 36 U.C.C. Rep. Serv. (Callaghan) 860 (Iowa Ct. App. 1982).

154. 105 Idaho 464, 670 P.2d 871, 37 U.C.C. Rep. Serv. (Callaghan) 478 (1983).

155. *Gillette Dairy, Inc. v. Mallard Mfg. Corp.*, 707 F.2d 351, 36 U.C.C. Rep. Serv. (Callaghan) 860 (8th Cir. 1983); *Beckenstein v. Potter & Carrier, Inc.*, 191 Conn. 150, 464 A.2d 18, 37 U.C.C. Rep. Serv. (Callaghan) 158 (1983). *But see* *Spring Motors Distribs., Inc. v. Ford Motor Co.*, 191 N.J. Super. 22, 465 A.2d 530, 37 U.C.C. Rep. Serv. (Callaghan) 62 (App. Div. 1983). Note that the New Jersey Supreme Court granted a request for a writ of certiorari, and its decision (not available at this writing) should clarify the law in New Jersey and be of guidance elsewhere.

exclusion of the jurisdiction's general limitations statute for breach of contract.<sup>166</sup> If personal injury is the result, the only discernible trend is towards uncertainty. Two federal district courts following the laws of Delaware<sup>167</sup> and Indiana<sup>168</sup> found each state's enactment of U.C.C. section 2-725 applicable. In contrast, federal courts employing the laws of Kansas<sup>169</sup> and Virginia<sup>160</sup> applied the state statute of limitations applicable to tort or personal injury actions. Opinion also continues divided on the proper statute of limitations when the action is for indemnity.<sup>161</sup>

Another aspect of U.C.C. section 2-725 involves the time of accrual of a cause of action for breach of warranty. Although the accrual date is normally when delivery is tendered, the Code also adopts a "time of discovery" rule "where a warranty explicitly extends to future performance . . . and discovery of the breach must await the time of such performance."<sup>162</sup> An express warranty that "[r]oof surface and installation shall be guaranteed unconditionally for a period of five years and any leakage occurring within that time shall be promptly repaired or replaced" was held to be such a warranty.<sup>163</sup> Confusing the concepts of warranty and remedy, the court then held that the cause of action did not arise when the leak was discovered but when it became apparent that the defendant would be unable to effectively repair or replace the roof.

Other decisions within this reporting period hold that neither a five-year guarantee,<sup>164</sup> nor the commitment to future repair or replacement,<sup>165</sup> constitutes a future warranty within the meaning of the U.C.C. section 2-725(2) exception.

156. *Transamerica Oil Corp. v. Lynes, Inc.*, 723 F.2d 758, 37 U.C.C. Rep. Serv. (Callaghan) 1076 (10th Cir. 1983).

157. *Sellon v. General Motors Corp.*, 571 F. Supp. 1094, 37 U.C.C. Rep. Serv. (Callaghan) 1169 (D. Del. 1983).

158. *Tolen v. A. H. Robins Co.*, 570 F. Supp. 1146, 37 U.C.C. Rep. Serv. (Callaghan) 790 (N.D. Ind. 1983).

159. *Thomas v. Heinrich Equip. Corp.*, 563 F. Supp. 152, 36 U.C.C. Rep. Serv. (Callaghan) 866 (D. Kan. 1983).

160. *Bly v. Otis Elevator Co.*, 713 F.2d 1040, 36 U.C.C. Rep. Serv. (Callaghan) 1569 (4th Cir. 1983).

161. *Compare Anixter Bros. v. Central Steel & Wire Co.*, 123 Ill. App. 3d 947, 463 N.E.2d 913, 39 U.C.C. Rep. Serv. (Callaghan) 28 (1984) (U.C.C. § 2-725 not applicable to implied contract indemnity actions; five-year "other civil action" statute applies), *with Perry v. Pioneer Wholesale Supply Co.*, 681 P.2d 214, 38 U.C.C. Rep. Serv. (Callaghan) 1274 (Utah 1984) (ultimate buyer's action is for breach of warranty; hence, indemnity action barred by U.C.C. § 2-725).

162. U.C.C. § 2-725(2).

163. *Smith v. Union Supply Co.*, 675 P.2d 333, 334, 37 U.C.C. Rep. Serv. (Callaghan) 795, 795 (Colo. Ct. App. 1983).

164. *Chicago Heights Venture v. Dynamit Nobel of Am., Inc.*, 575 F. Supp. 214, 37 U.C.C. Rep. Serv. (Callaghan) 1109 (N.D. Ill. 1983).

165. *Ontario Hydro v. Zallea Sys., Inc.*, 569 F. Supp. 1261, 1266, 36 U.C.C. Rep. Serv. (Callaghan) 1222, 1228 (D. Del. 1983) ("Thus, the key distinction between these two kinds of warranties is that a repair or replacement warranty merely provides a *remedy* if the product becomes defective, while a warranty for future performance *guarantees the performance* of the product itself for a stated period of time") (emphasis in original).

Furthermore, the requirements for a future performance warranty were not met by General Motors' warranty: "To help protect you, every Olds provides all this for occupant protection . . . Fuel Tank impact security."<sup>166</sup>

## BULK TRANSFERS

In those states that have adopted optional U.C.C. section 6-106, one problem is how to distribute the proceeds of sale if they are insufficient to pay all claims in full. Section 6-106(3) provides that "distribution shall be made pro rata." In *William Iselin & Co. v. Delta Auction & Real Estate Co.*,<sup>167</sup> the court did not apply this language literally and ruled that secured and judicial lien creditors are entitled to priority in a distribution of proceeds.<sup>168</sup> Assuming that the original judicial lien also extends to proceeds, as does a security interest,<sup>169</sup> the court's conclusion seems correct.<sup>170</sup> There is no evidence that the drafters of article 6 intended to alter existing priority schemes.

In *In re Radcliffe's Warehouse Sales, Inc.*,<sup>171</sup> the Bankruptcy Court for the Western District of Washington held that section 108 of the Bankruptcy Code did not extend the time for the trustee of the transferor to sue the transferee to set aside a noncomplying bulk transfer. In reaching this conclusion, the court disapproved of *In re Curtina International, Inc.*<sup>172</sup> and held that section 108(a) did not apply because the right being asserted against the transferee is a right of the creditors of the transferor/debtor, not the right of the debtor itself. Although this is true, the trustee acquires his cause of action pursuant to section 544(b) of the Bankruptcy Code, and section 546(a) gives the trustee two years within which to sue. This should preempt the shorter article 6 period. Unfortunately, the court in *Radcliffe's* did not discuss sections 544(b) and 546, and the court in *Curtina* wrongly said that section 546 did not apply while section 108(a) did.

Two cases involved the scope of article 6. In one the Virginia Supreme Court held an enterprise not subject to article 6 because, despite an extensive inventory of replacement parts, its principal business was repairing radiators, a service,

166. *Sellon v. General Motors Corp.*, 571 F. Supp. 1094, 1097, 37 U.C.C. Rep. Serv. (Callaghan) 1169, 1172 (D. Del. 1983).

167. 433 So. 2d 911, 36 U.C.C. Rep. Serv. (Callaghan) 607 (Miss. 1983).

168. *Accord Huguelet v. M & M Assocs.*, 375 So. 2d 1150, 27 U.C.C. Rep. Serv. (Callaghan) 1091 (Fla. Dist. Ct. App. 1979); *Bomanzi of Lexington, Inc. v. Tafel*, 415 S.W.2d 627, 4 U.C.C. Rep. Serv. (Callaghan) 588 (Ky. 1967); *In re Bulk Sale of Clement*, 98 Dauph. 55, 71 Pa. D. & C.2d 717, 18 U.C.C. Rep. Serv. (Callaghan) 1280 (C.P. 1976).

169. See U.C.C. § 9-306(2).

170. At least one member of the subcommittee feels that theoretically § 6-106(3) should be applied literally because the secured creditor can still foreclose on the collateral once it is in the transferee's hands and, therefore, does not need to be given preferential treatment in the distribution of the proceeds. Another member believes that the treatment should depend on whether the bulk sales price was reduced by the secured debt, that is, whether the bulk sale was "under and subject" or not.

171. 31 Bankr. 827, 36 U.C.C. Rep. Serv. (Callaghan) 915 (Bankr. W.D. Wash. 1983).

172. 23 Bankr. 969, 34 U.C.C. Rep. Serv. (Callaghan) 1311 (Bankr. S.D.N.Y. 1982).

and not the sale of merchandise from stock.<sup>173</sup> The other case involved a sale of fixed assets and an option to purchase the inventory at a future date. There was no compliance with article 6, but the transferee agreed to pay a secured party some of the outstanding balance owed by the debtor. The court ruled that the bulk transfer article does not regulate an agreement to sell inventory in the future. Until sold, the inventory remains subject to the vendor's creditors. Alternatively, a sale for the benefit of the secured party would also be exempt even if to a third person by the debtor.<sup>174</sup>

### ***WAREHOUSE RECEIPTS, BILLS OF LADING, AND OTHER DOCUMENTS OF TITLE***

There were no startlingly significant decisions under article 7.

173. *Allsbrook v. Azalea Radiator Serv., Inc.*, 316 S.E.2d 743, 38 U.C.C. Rep. Serv. (Callaghan) 1714 (Va. 1984).

174. *Ouachita Elec. Co-op v. Evans-St. Clair*, 12 Ark. App. 171, 672 S.W.2d 660, 39 U.C.C. Rep. Serv. (Callaghan) 640 (1984).

